**BEFORE THE PUBLIC UTILITIES COMMISSION**

**OF THE STATE OF CALIFORNIA**

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# TURN'S PRE-WORKSHOP COMMENTS ON THE IMPLEMENTATION OF SB 1036


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Pursuant to the direction provided by Executive Director Paul Clanon in his letter dated April 24, 2008, and the further direction provided by Energy Division in its request for pre-workshop comments, TURN provides the following comments on certain issues pertaining to the implementation of SB 1036.

TURN strongly supports the introductory comments made by Energy Division, which explain that the statutory language prescribes that "the [above-MPR] funds are limited and once the funds are exhausted, the large IOUs are relieved of their above-MPR RPS procurement obligations."[1] The Commission should carefully weigh the standards that will be used to disburse the funds available to cover above-MPR costs so as to "maximize renewable energy development and ratepayer benefits in California."

TURN first provides some general comments on the proposal presented in Draft Resolution E-4160 and then answers some of the questions posed in the Staff Request for Comments.

## A. Comments on Staff Proposal in Draft Resolution E-4160

1. <u>Eligibility criteria</u>

In Draft Resolution E-4160 staff proposed certain additional "eligibility criteria" for projects to qualify for AMF funds and provided detailed reasonableness standards for reviewing projects which might qualify for such funding. The underlying rationale for establishing such standards was "to promote the efficient use of limited above-market

[1] Public Utilities Code Section 399.15 (d) (3)

funds in a manner that maximizes ratepayer benefit." (DR E-4160, p. 20). TURN strongly agrees with this rationale. The amount of AMFs is currently statutorily limited to approximately $773,000,000.[2] TURN agrees that this amount could easily be spent on a few very expensive projects. While §399.15(2) imposes some criteria for projects to qualify for AMFs, those criteria generally mimic the requirements of the renewable procurement plan in §399.14.[3] However, rather than simply spending this money on a "first come, first served" basis, it is entirely appropriate for the Commission to ensure that the funds are used to support the most cost-effective and viable renewable energy projects.

The primary additional proposed eligibility requirements are that the project be "physically located in California," and that the funds not be used for "firming and shaping costs" to bring in out of state intermittent renewable energy. This requirement is consistent with the overall legislative intent of the RPS statute. While the definition of "in-state" renewable projects includes renewable energy "delivered" to California, such out-of-state imports do not have the same characteristics as in-state projects. Specifically, the RPS statute, in Section 399.11 of the Public Utilities Code, expresses the legislative intent to promote not only the "regional" benefits of renewable power, but also the environmental and economic benefits of local projects and the economic benefit of price stability.[4] Out of state projects do not produce local jobs and do not necessarily reduce noxious air emissions in California. Paying additional costs for "firming and

[2] TURN recognizes that the legislature could decide to increase this amount by extending the current January 1, 2012, termination date for the accrual of dollars to fund AMFs.

[3] The primary difference is that there is no exception for shorter term (less than 10 years) contracts.

[4] See also, Public Resources Code, Section 25740.5(c).

shaping," especially if the underlying energy is priced at an index price, does not promote price stability.

2. <u>Reasonableness criteria</u>

The draft resolution identifies five reasonableness criteria for projects which require AMFs less than $5,000,000. (DR E-4160, p. 20-21). These standards will promote the selection of projects that not only compare favorably on an economic basis but also show a higher probability of success.

Several parties expressed concern regarding the proposal that the Commission have "discretion to use another COD (and thus, MPR) if the project's COD estimate is not reasonable." (DR E-4160, p. 21). The practical impact of this recommendation is that *if* the Commission selects a later COD, the MPR will be different, although one cannot *a priori* predict whether the MPR for a later on-line date (assuming same year's MPR) would be higher or lower.

The fifth criterion suggested by staff is a project-specific evaluation by the Independent Evaluator that includes a review of the "proposed project's financial model." The history of renewables solicitations indicates a recurring problem with long development timelines and overly optimistic pricing terms. A review by the IE of the project's financial modeling may provide a valuable "reality check" on the project's bid.

Both PG&E and SCE argued that certain of the reasonableness criteria conflict with the realities of renewable project development, noting that developers may not be able to get the financing necessary to secure site control or complete transmission studies prior to first securing an approved PPA. TURN agrees that these concerns merit further discussion in the upcoming workshop, but takes no position at this time on whether or not the criteria should be changed.

3. Additional conditions

The draft resolution recommended that the Commission retain the ability to reduce or terminate AMFs dedicated to a project if the project failed to meet required contract milestones. (DR E-4160, p. 23). This condition is yet another attempt to ensure that AMFs are reserved for viable projects and are not tied up with projects that may not succeed. SCE points out that this provision would increase ratepayer costs, apparently on the assumption that the utility would still honor the contract but simply not count the above-MPR costs toward the AMF cost cap.

Obviously, it makes no sense to continue pursuing a project once AMF funding is revoked, and the more logical assumption is that the utility would need to exercise its contractual right to terminate the project for failure to meet required milestones. However, this issue should be clarified and TURN looks forward to further discussion at the workshop.

Likewise, the draft resolution requires that contracts seeking amendments – especially price renegotiations – provide additional information, including a list of project costs, financial models and documentation of price increases. (DR E-4160, p. 22). The utilities in their comments complain that these requirements are too onerous and will have a "chilling effect" on solicitations.

TURN strongly supports the proposed requirements. Projects which are selected based on a careful review of their bids should not allowed to easily come in for price increases. That is the whole point of the competitive solicitation. This is not a novel approach. The utilities sometimes use "open book" review during renegotiations of conventional PPAs. If the developer is unwilling to justify a material change in the project terms, the contract should be allowed to terminate.

## B. Response to Specific Questions Posed by Staff

1. *The cost limitations established by SB 1036 involve summing funds that would have been collected over several years. SB 1036 does not suggest that a discount rate should be applied to the calculation of the limit. Yet, the funds do impose real costs and benefits on various stakeholders, each with a different perspective on the time value of money.*
   - *Discuss whether a discount rate should be applied to the cost limitation calculation.*
   - *Absent SB 1036, would the PGC funds collected have been subject to financing charges, interest payments or a discount rate that would directly or indirectly affect the cost limitations? If yes, please cite the legislation, documentation, precedent, or practice on which you base your answer.*
   - *Please provide a spreadsheet calculation (and all supporting documentation) if you propose a calculation that differs from the calculation proposed in Draft Resolution E-4160.*
2. *Attached to this Pre-Workshop Comment Request is the Staff's proposed AMFs Calculator. Prior to SB 1036, the CEC's proposed method for calculating above-market costs was to calculate the difference between the levelized bid price and the applicable levelized MPR. The nominal sum of that difference represented the total amount of SEP funds requested by the generator, and was then to be paid over the life of the contract. With SB 1036, funds for AMFs will not be collected up-front through the public goods charge, but rather will be recovered in utility rates.*
   - *Should a discount rate be applied to the AMFs request of an RPS contract? If so, should the discount rate be the utility's authorized WACC or another discount rate? Please provide a credible public source of data for establishing another discount rate.*

Both PG&E and SCE expressed concerns in their comments on DR 4160-E regarding the particular calculations proposed by staff. TURN very much shares those concerns. The staff approach would essentially compare the *nominal* amount of dollars collected to fund AMFs with the *discounted* amounts to be paid out from those funds.

This is a fundamental error. In order to make a valid comparison between two streams of dollars, those streams must be converted to a common basis and expressed in constant dollar terms. Whether the discount rate is the utility's Weighted Average Cost of Capital, as staff suggests, or the GDP deflator, as PG&E recommends, it is clear that both sides of the ledger must be expressed in the same terms. However, TURN prefers the PG&E approach of using the GDP deflator, because it is generally consistent with the escalation that applies to the collection of Public Goods Charge programs.

TURN does *not* support SCE's "simple cash flow analysis," because that approach ignores the fact that AMFs may be *committed* for many years into the future. Simply waiting until the "checkbook" is empty, to use SCE's terminology, will result in unfunded AMF liabilities in future years when no more funds are available. Future AMF payouts must be taken into account in determining when the funds have been exhausted

3. *Comment on whether contracts with prolonged negotiations (e.g. the contract is executed more than 18 months since the close of the solicitation in which it bid) or projects that have significantly changed since the original bid should be considered bilateral contracts and thus not eligible for AMFs.*

TURN suggests that the standard of review for any contract that is priced above the applicable MPR should employ the same criteria, as discussed further in response to Question 8. Thus, the categorization of the contract should not matter.

4. *Identify what is the appropriate MPR to calculate an AMFs request for a contract in each of the following situations:*
    - *With prolonged negotiations (e.g. a contract executed more than 18 months after the close of the solicitation);*

In order to prevent gaming opportunities, such as deliberate delay in order to fall below a future MPR, the appropriate MPR should be based on the year in which the project was bid into a competitive solicitation, or the year in which the bilateral contract proposal was first submitted.. In other words, the MPR vintage date should be established when the project is first proposed.

- *That has been previously approved, but is requesting a price amendment;*

Same response as above.

- *With an expected commercial online date that is unrealistic given expected transmission upgrade needs.*

TURN suggests that the utilities should ensure that projected contract online dates (which determine the appropriate MPR) are realistic in the first instance.

5. *Discuss whether the following proposed eligibility criteria promote the efficient use of limited AMFs in a manner that maximizes benefits for ratepayers, shareholders, and the RPS Program:*

TURN addressed most of these issues in our comments above.

- *The contract price is an all-in fixed price for a bundled energy product from a RPS-eligible facility;*

Yes. The MPR represents an all-in fixed price, so contracts that are priced in a way that prevents a valid comparison should not be authorized. In particular, contracts that are indexed to current power market prices should not be authorized, since one of the goals of the RPS legislation was to promote the price stability that comes with fixed-price renewable contracts. TURN can envision allowing a certain limited exception for short term contracts, when the utility can demonstrate that the contract cost plus any additional hedging costs are still below the applicable MPR.

- *The contract is with an RPS-eligible facility that is physically located in California;*
- *The project is not otherwise eligible for other Commission-approved funding programs (e.g. Application 07-07-015 pending Commission approval for Emerging Renewable Resource Program (ERRP));*
- *The AMFs request cannot include firming and shaping costs.*

6. *Discuss how a "true-up"[5] of awarded AMFs will or will not affect the financing for a RPS project.*
7. *Identify any material factual disputes that may require an evidentiary hearing.*
8. *Draft Resolution E-4160 proposed review standards for contracts with above-MPR costs. In comments, a number of parties questioned whether the Commission review standards should be consistently applied to all contracts. Below is a list of different RPS contract types the Commission reviews. Please comment on whether the Commission should review the following types of renewable contracts using the same or varying review standards. If varying review standards should be used, please provide rationale for using different standards and identify which review standards should apply to which contract types.*
   - *Contracts negotiated as part of a competitive solicitation*
   - *Bilateral contracts*
   - *Short-term contracts*
   - *Long-term contracts*
   - *Contracts with prices greater than the MPR*
   - *Contracts with prices below the MPR*
   - *Projects smaller than ~20 MW*
   - *Utility-scale projects (~ greater than 20 MW)*
   - *New or repowered generation*
   - *Existing generation*
   - *Wholesale distributed generation*
   - *Technologies that have not been commercially demonstrated*
   - *Contracts that are eligible for AMFs*
   - *Contracts ineligible for AMFs*
   - *AMF need is $1,000,000*
   - *AMF need is $70,000,000*

Contracts with prices above the MPR

TURN fully agrees with CLECA, which explained in its comments on the draft resolution why the Commission should use the same standards to evaluate above-MPR contracts irrespective of whether they were negotiated bilaterally or through the competitive solicitation process. CLECA argued that a more stringent standard for

[5] If a project's actual online date differs from the expected online date in the contract, it would likely require a different amount of AMFs.

contracts qualifying for AMFs (i.e. competitive bids) would result in the utility favoring bilateral contracts and would thus undermine the competitive solicitation process.

The ALJ in R.06-02-012 issued a Ruling requesting comments on this issue back in May of 2007. Comments were filed in June of 2007. This was *prior* to the passage of SB 1036. The passage of SB 1036 only increases the need to closely scrutinize bilateral contracts. Prior to SB 1036 the utilities transferred PGC funds to the SEP account at the CEC, which they had collected through the mandated public purpose surcharge. Contracts qualifying for SEPs (*i.e.*, signed through the competitive solicitation process) allowed the utility to recover funds they had already collected in rates out of this statewide pool. Thus, the utility had a clear incentive to ensure that any above-market contracts that they entered into would be eligible for SEPs. Under the current system, the impact to utility rates is the same irrespective of whether the contract is a bilateral (does not qualify for AMFs) or a competitive bid (qualifying for AMFs). In this situation, the utility has an incentive to *favor* a bilateral contract to the extent that its motivation to purchase more renewables exceeds its motivation to take advantage of the AMF cost cap.

In our June 2007 comments TURN recommended that bilateral contract pricing should be reasonable in comparison to the bid curves from the competitive solicitation. TURN also recommended that the Commission should limit the ‘above-market’ costs for bilateral contracts, irrespective of the fact that those contracts did not qualify for SEPs. In essence, bilateral contracts priced above the MPR represent another pool of funds available to subsidize renewable energy projects. The Commission should ensure that such projects meet at least the same reasonableness criteria as projects which have gone through the competitive solicitation. If anything, contracts that do not qualify for AMFs should be subject to stricter scrutiny than those that do.

Projects below the MPR

The draft resolution proposed more stringent criteria for projects that qualify for AMFs. TURN appreciates the concern raised by SCE as to why a contract for a price just above the MPR should be treated differently than a project with a price just below the MPR. Ideally, the level of review should depend on the level of ratepayer exposure, which is determined by the combination of the price, term and size of the project. Ratepayer exposure to total contract costs above a certain amount should warrant greater scrutiny, although any fixed criteria will require some cutoff figure that could be criticized. One needs only to look at the number of power plants with capacities of just below 50 MW for an example of this effect.

However, the RPS statute defines the MPR as the "cutoff" number that leads to the use of AMFs, and ultimately provides some limit on total ratepayer funding for renewable energy. The California legislature and the CPUC have determined that ratepayers should subsidize renewable energy by calculating a long-term fixed price which includes long term capital costs and an estimate of long-term fuel costs, as well as an adder for GHG costs. However, the legislature has also determined that *ratepayers should not pay for renewable energy at any cost*, thus establishing a different level of scrutiny for projects above the MPR that qualify for limited AMFs.

## C. Conclusion

TURN appreciates the opportunity to submit these comments and looks forward to participating in the upcoming workshop.

Respectfully submitted,

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